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No. 84-1031

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1984

COMMUNICATIONS SATELLITE CORPORATION,
Appellant,

VS.

FRANCHISE TAX BOARD,
Appellee.

APPELLEE'S MOTION TO DISMISS OR AFFIRM

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QUESTION PRESENTED

Does the unique fact that Comsat makes use of property located in outer space warrant a departure from accepted principles which call for apportionment of business income among those jurisdictions where a corporation conducts its business activities?

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Appellee, pursuant to Rule 16 of the Rules of the Supreme Court of the United States, hereby moves this Court to dismiss this appeal or to affirm the judgment of the Court of Appeal of the State of California on the ground that this case does not present a substantial federal question.

INTRODUCTORY STATEMENT

In its presentation to this Court, appellant ("Comsat") has studiously avoided any mention of the fundamental issue raised by the facts of this case. That issue is whether California has violated any constitutional principles by employing an apportionment formula which does not assign any of Comsat's income to outer space, but instead apportions Comsat's income among those jurisdictions where it conducts its business activities. Prior decisions of this Court make it clear that use of such a formula by the California taxing authorities is constitutionally permissible. A full-scale review of the challenged state court decision is therefore unnecessary.

Comsat is the United States participant in the International Telecommunications Satellite Consortium ("Intelsat"), an international joint venture which operates a global satellite communications system. The satellites and other space segment assets of the system are owned in undivided shares by members of Intelsat, including Comsat, in varying percentages. Comsat also owns a 100 percent interest in an earth station located in Talkeenta, Alaska, and a 50 percent interest in seven other U.S. earth stations in the Intelsat system, including one at Jamesburg, California.

Intelsat leases satellite capacity to Comsat. Comsat, in turn, derives its principal revenues from the leasing of half circuits (two-way communication channels between satellites and earth stations) to a number of terrestrial communication carriers. During the years in question, Comsat also received approximately 52.5 percent of Intelsat's gross revenues by reason of its equivalent ownership interest in the space segment assets of the system.

Comsat contends that it earns a substantial portion of its income in outer space where the Intelsat satellites are located, and thus the values associated with the satellites should be attributed to outer space. The Franchise Tax Board of the State of California ("the Board") contends that Comsat earns its income "here," not "up there" in the tax-free blue yonder. It accordingly has assigned a portion of Comsat's revenues associated with the satellites to California, the site of one of the eight U.S. earth stations which communicate with the satellites. As previously indicated, the overall effect of the Board's formula is to apportion Comsat's income among those jurisdictions in which Comsat is engaged in business.

In Comsat's view, a formula which does not assign any of its income to outer space is constitutionally defective

because it necessarily results in the taxation of "extraterritorial" values. Comsat, however, is not engaged in commerce with unnamed creatures in outer space, but with such Earthlings as American Telephone and Telegraph Company. Its activities in the hostile environment of outer space have value only on Earth. And it is here on Earth that various jurisdictions, including California, provide the protections and services which enable Comsat to function and profit as a business concern.

Comsat has also failed to recognize that the apportionment concept has been developed and applied as a means of avoiding duplicative taxation where each of two or more jurisdictions has a valid basis for asserting the power to tax. It therefore makes little sense to apply the apportionment concept in a manner which immunizes a corporation's income from taxation by *any* jurisdiction. Comsat is seeking to do just that by including the fictional "jurisdiction" of outer space in its equation.

THE OPPOSING FORMULAS

The apportionment formulas employed by the respective parties basically differ, of course, in that Comsat's formula assigns income to outer space while the Board's formula does not. This basic difference in approach is at the heart of the controversy, and the manner in which each party has computed the resulting tax liability under the two approaches is really quite secondary. Nevertheless, a number of inaccuracies in Comsat's description of the opposing formulas cannot go uncorrected.

It is asserted that "Comsat computed its tax liability by the statutory formula for the years at issue (1970-72)" and that the Board used "a 'special formula' wholly different from the statutory three-factor formula." Juris.

Stmt., at 6, 7.[1] These assertions are in direct conflict with the holdings of the California appellate court that (1) Comsat did *not* compute its California income in accordance with the statutory formula, and (2) the Board's formula, though denominated a "special formula," was consistent with the statutory formula. See Juris. Stmt. App. A-28 through A-33.

A. The Property Factor

With respect to the property factor of the statutory formula, section 25129 provides that "the numerator of [the factor] is the average value of the taxpayer's real and tangible personal property owned or rented and *used* in this state." (Emphasis added.) Prior to trial, the parties entered into a stipulation of facts in which it was agreed that "In each of the years in question, Comsat computed the property factor according to the fraction prescribed by section 25129 of the Code." Stip., ¶ 43. They further stipulated that "the numerator equalled, at original cost, Comsat's interest in California property in service (consisting of the California earth station and the engineering office in Los Angeles County)." *Id.* In answering interrogatories propounded by Comsat, the Board also stated that "The property factor employed by the Board to apportion plaintiff's income differs from the property factor described in section 25129 in that it includes property not located in this state...." Pl. Exh. 2.

Both parties, in short, read the definition of the numerator of the property factor in section 25129 as referring to property physically located in California. The Board,

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[1] The controlling statutory provisions are contained in the Uniform Division of Income for Tax Purposes Act ("UDITPA"), enacted in California in 1966 as sections 25120 et seq. of the California Revenue and Taxation Code. All statutory references in this motion are to the California code sections incorporating UDITPA unless otherwise noted.

however, consistently argued in the lower courts that the satellites were actually "used" in California for the production of income, not in the physical sense, but as a matter of business reality.

The Court of Appeal agreed with the Board's argument that the satellites were indeed "used" in California, but it disagreed with the parties' construction of section 25129. The court said:

> "The pertinent language of section 25129 defining the numerator of the property factor refers to property 'owned' and 'used' in this state, not to property 'located' here. Moreover, the satellites are not located in California but the Jamesburg earth station is. Because it is, Comsat is conducting 'business activity' and generating income in California. There is an invisible, but apparently continuous and very real, connection between the earth station and the satellites. The earth station has a value only because this connection exists, and it is otherwise of no value. Without the connection, the satellites function in outer space to no purpose involving this state. With it, they function in California. The ascription of a 'function in California' to the satellites is a recognition of the realities of telecommunications and space technology, not an indulgence in fiction." Juris. Stmt. App. A-28 to A-29.

The court went on to conclude that the satellites "are 'tangible personal property owned . . . and used in this state,' by Comsat, within the meaning of section 25129." *Id.*, at App. A-29.

B. The Sales Factor

The Court of Appeal also concluded that Comsat's sales factor differed from the factor set forth in the statute. The sales factor prescribed by UDITPA is generally

defined as a "fraction, the numerator of which is the total sales of the taxpayer in this state during the income year, and the denominator of which is the total sales of the taxpayer everywhere during the income year." Cal. Rev. & Tax. Code § 25134. With respect to the numerator of the factor, section 25136 further provides:

> "Sales, other than sales of tangible personal property, are in this state if:
>
> (a) The income-producing activity is performed in this state; or
>
> (b) The income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance." [2]

During the years in question, the Board's interpretation of the above provision was contained in Regulation 25136(e)(2) (18 Cal. Admin. Code § 25136(e)(2)). This Regulation provided, in relevant part, as follows:

> "Except as provided by special apportionment formulas (including special formulas the use of which has been continued or adopted by the Franchise Tax Board since enactment of Sections 25120 to 25139, inclusive), receipts from sales other than sales of tangible personal property which constitute a principal source of business income shall be attributed to this state in accordance with the following:
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> * * *

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[2] Although the California court held that Comsat's formula did not comply with these statutory provisions, see Juris. Stmt. App. A-30 to A-33, Comsat has not included section 25136 in its listing of relevant statutes and has neglected to quote its provisions in the Appendix to its Jurisdictional Statement.

> "(B) Gross receipts from the rental, lease, licensing the use of or other use of tangible personal property shall be assigned to this state if the property is within the state during the entire period of rental, lease, license or other use. If the property is within and without this state during such period, gross receipts attributable to this state shall be based upon the time which the property was physically present or was used in this state bears to the total value or use of the property everywhere during such period."

The parties have never seen eye-to-eye on which of their respective sales factors more closely approximates the statutory factor, and there was no stipulation on this subject. Comsat used a numerator which reflected a so-called "ground percentage" of the revenue which Comsat received from the leasing of half circuits through the California earth station, plus certain incidental rental income received from the rental of space at the earth station site to others. Juris. Stmt. App. A-30; Stip., ¶¶ 47, 48. Since the half circuits were leased at a single charge, see Stip., ¶ 33, Comsat had to arrive at a figure representing the "ground percentage" purportedly attributable to the earth station alone.[3] This was done through use of a special subformula based on Comsat's

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[3] Comsat claims to have relied on Regulation 25136(e)(2)(B) in taking this approach, Juris. Stmt., at 6, but whether Comsat was even aware of the Regulation at the time it filed its returns is not a matter of record. In any event, the Regulation clearly does not apply in this situation. The first sentence deals with receipts from the use of property solely within the state. In the leasing of half circuits, Comsat does not derive its receipts from the use of property solely within the state, but from the use of property located within California (the earth station) and the use of property located outside California (the satellites). The second sentence of the Regulation deals with receipts from the use of property which is "within and without this state during [the] period [of use]," and provides that the receipts from such use shall be

relative investment in the satellites and the earth station. Stip., ¶48. Such a special subformula is not prescribed by *any* statute. See Juris. Stmt. App. A-31.[4]

The Board used a sales factor which differed from Comsat's in two respects: (1) it assigned all receipts from half circuits through the California earth station to California, and (2) it attributed a portion of Comsat's revenue from Intelsat to California. Prior to trial, in answering the interrogatories propounded by Comsat, the Board stated that this factor differed from the sales factor described in section 25134 and Regulation 25136(e)(2)(B)[5] "in that it includes receipts from the rental or other use of tangible personal property located outside this state. . . ." Pl. Exh. 2. The Board urged in

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determined on a time-ratio basis. It is impossible to determine California receipts from Comsat's activity on a time-ratio basis since its activity involves property which is never "within *and* without" the state—i.e., the earth station is always in California and the satellites are always in outer space.

Faced with this difficulty of bringing its operations within the express terms of the Regulation, Comsat attempts to create the impression that its lease of half circuits is not a single income-producing activity, but entails *two* income-producing activities: "the lease of the use of the California earth station" and "the lease of the use of a satellite." Juris. Stmt., at 6. This characterization of Comsat's leasing activity conflicts with its statutory authorization to "furnish for hire, *channels of communication* to United States communication carriers and to other authorized entities, foreign and domestic." 47 U.S.C.A. § 735(a)(2); emphasis added. Comsat does not lease satellites and earth station facilities; it leases half circuits between the two elements.

[4] Even records separately stating *total* revenues from half circuits through the California earth station were not available for 1970 and 1971. Stip., ¶ 48. Thus, for those years, Comsat was forced to calculate the revenues from these half circuits by means of still another formula. *Id.*

[5] The Regulation was improperly cited in the answer to interrogatories as "Regulation 25136(*b*)(2)(B)."

the lower courts, however, that its sales factor was consistent with section 25136, subdivision (b), which provides that "Sales . . . are in [California]" if "a greater proportion of the income-producing activity is performed in this state *than in any other state.* . . ." (Emphasis added.)[6]

The Court of Appeals held, in effect, that the numerator of the Board's sales factor was consistent with subdivision (*a*) of section 25136. It pointed out that section 25136 defines "the term 'sales of the taxpayer in this state' with reference to the location of the 'income-producing activity' in California [subdivision (a)] or its location as between California and 'any other state' [subdivision (b)]." Juris. Stmt. App. A-30. The court went on to conclude:

> "The Board's numerator included part of the revenue Comsat had derived from leasing half circuits. That part was properly characterized as Comsat's 'sales in this state' because the 'income-producing activity' which generated it was the leasing of half

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[6] In the courts below, the Board took the position that since the apportionment provisions of UDITPA come into play only when a taxpayer is "taxable both within and without the state," Cal. Rev. & Tax. Code § 25121, it necessarily follows that income is to be apportioned only among the states in which the taxpayer conducts its business activity and is amenable to taxation. If, for example, Comsat were organized and operated for the sole purpose of providing a satellite communications system for the State of California, and it engaged in no activities in any other state, it would not be permitted to apportion its income under UDITPA because it would not be taxable elsewhere. It logically follows that any income which Comsat may derive from the use of satellites located in outer space should not be immune from tax simply because Comsat conducts its business in such a fashion that apportionment of its income between two or more jurisdictions is required. The Court of Appeal did not expressly consider what the Board has termed the "full taxability concept" in view of its holding that the satellites function in California and the income-producing activities in connection with the satellites occur in California.

> circuits at the California earth station: i.e., the activity was 'performed in this state' within the meaning of section 25136, subdivision (a). [Citation omitted.] The balance of the numerator was part of the satellite revenue Comsat received from Intelsat. The 'income-producing activity' which generated that revenue was the operation of the satellites themselves. Because they actually 'function' at the California earth station (as we have seen), their 'income-producing activity' is also 'performed in this state' within the meaning of section 25136, subdivision (a). For that reason, the part of Comsat's 'sales' representing revenue from their use was properly characterized as its 'sales in this state' within the same meaning." Juris. Stmt. App. A-32 to A-33.

C. Summary of Results.

The formula employed by the Board apportions approximately 8.9 percent of Comsat's income to California for the years in question, as compared with approximately 3.8 percent apportioned to California under the formula used by Comsat. Juris. Stmt. App. A-20, n. 10. During these same years, however, *between 16 and 19 percent of the total half circuits leased by Comsat were through the California earth station.* Stip., ¶ 37. Thus, at least insofar as it is appropriate to apportion Comsat's income among those jurisdictions where it is engaged in business activities, the formula employed by the Board obviously is a fair one.

It should also be evident from the above that, contrary to Comsat's assertions, the comparative figures of 3.8 and 8.9 percent do not reflect a discrepancy between results obtained under the statutory formula and the so-called

"special formula" of the Board.[7] The figures that are labeled "statutory" in the summary at page 8 of Comsat's Jurisdictional Statement are *Comsat's figures*, based on how *Comsat* believes the corporation should be taxed. See, e.g., the Court of Appeal's labeling of the same summary at Juris. Stmt. App. A-20, n. 10.

Finally, Comsat has not been entirely candid with the Court in describing the numerator of the Board's sales factor. It states that a subfactor used by the Board to determine California revenue consisted of "Earth Station Revenue" plus "Space Segment Revenue" plus "Intelsat Revenue." Juris. Stmt., at 8. The clear implication is that the Board considered "Earth Station Revenue" and "Space Segment Revenue" to be divisible, and that it had actually arrived at separate figures for each "type of revenue." This, of course, was not the case. A breakdown of revenues purportedly attributable to the earth station, on the one hand, and the satellites, on the other, was made only by Comsat. See *supra*, at 7-8. As stipulated by the parties, the Board's subfactor consisted of "Revenue

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[7] Moreover, while the standard three-factor formula is generally workable, it clearly is not appropriate in every situation. Accordingly, UDITPA includes a relief provision authorizing the employment of a "special formula" when the standard formula does not properly reflect the income attributable to the taxing jurisdiction. See Cal. Rev. & Tax. Code § 25137. It follows that whether the Board employed a "special formula" in reapportioning Comsat's income, or brought Comsat into line with the prescribed elements of the statutory formula, is really beside the point. As the Court of Appeal concluded, a portion of the income which Comsat derives from the use of the satellites is attributable to its business activities in California. Assuming that Comsat is correct in insisting that such income cannot be apportioned to California under the statutory formula, then employment of a "special formula" under section 25137 is proper. The result is the same either way.

from Intelsat" plus "Revenue from rental of all half circuits." Stip., ¶61; see also Juris. Stmt. App. A-19.[8]

ARGUMENT

I

COMSAT'S DUE PROCESS CLAIMS ARE INCONSISTENT WITH THE APPORTIONMENT CONCEPT LONG APPROVED BY THIS COURT.

Comsat's notion that a substantial portion of its income should be attributed to outer space not only defies common sense but is plainly at odds with the apportionment concept as it has been developed and applied by this Court. Where a multistate corporation derives its income from a unitary business "the income bears relation to benefits and privileges conferred by several States" and "apportionment is ordinarily the accepted method" of allocating that income among those states where the unitary business is conducted. *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 445 (1980). As recently explained in *Container Corp. of America v. Franchise Tax Board*, ____ U.S. ____, 103 S.Ct. 2933, 2940 (1983):

> "...The unitary business/apportionment method is a very different approach [than geographical or transactional accounting] to the problem *of taxing*

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[8] In order to pave the way for a later legal argument, see Juris. Stmt., at 17-18, Comsat has also described the operation of the California earth station in terms different from those used in the parties' stipulation of facts. Comsat states, for example, that "communications from offshore U.S. points and foreign countries are received via satellites by the California earth station *which...continues their transmission to points of destination elsewhere in the United States.*" Juris. Stmt., at 5; emphasis added. Actually, as the parties stipulated, such communications "are received via satellite by the California earth station and are then transmitted to their point of destination in the United States through terrestrial facilities owned and operated by communication common carriers other than Comsat." Stip., ¶ 24.

> *businesses operating in more than one jurisdiction.* It rejects geographical or transactional accounting, and instead calculates the local tax base by first defining the scope of the 'unitary business' of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of that 'unitary business' between the taxing jurisdiction and the rest of the world on the basis of a formula taking into account objective measures of the corporation's activities within and without the jurisdiction." (Emphasis added.)

Thus, this Court continued:

> "...The first, and ... obvious, component of fairness in an apportionment formula is what might be called internal consistency—that is the formula must be such that, *if applied by every jurisdiction, it would result in no more than all of the unitary business's income being taxed." Id.,* at 2942; emphasis added.

The apportionment concept therefore presupposes multiple jurisdiction to tax.[9] And one of its obvious objectives is to minimize the prospect of duplicative taxation where a corporation has extended its activities beyond the confines of a single jurisdiction.

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[9] This is explicitly recognized in proposed regulations issued by the Multistate Tax Commission for use by the states which have adopted UDITPA either directly or through membership in the Multistate Tax Compact. Regulation IV.2(a)(2) of the Commission, adopted in California as 18 Cal. Admin. Code §25121(a)(2), provides that " 'Apportionment refers to the division of income *between states* by use of a formula containing apportionment factors." (Emphasis added.) "State" is defined in the Uniform Act as "any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, and any foreign country or political subdivision thereof." Cal. Rev. & Tax. Code §25120(f).

Comsat takes the view that the apportionment concept cannot be given its usual effect here because, under the facts of this case, the concept conflicts with the established " 'general principle' . . . that 'a State may not tax value earned outside its borders.' " Juris. Stmt., at 12.[10] In taking this stance, Comsat erroneously assumes two things: (1) that the values it is talking about actually have their source in outer space, and (2) that, even assuming some values are produced in outer space, it is constitutionally required that such values be assigned to outer space for tax purposes.

A. The values associated with the satellites are produced on Earth

It cannot be said that extraterritorial values are being taxed unless those values are produced extraterritorially. In the present case, the man-made satellites in the Intelsat system have been placed in outer space to serve the needs of Earthlings. Without the earth stations, they would be useless pieces of sophisticated hardware floating around in outer space with no function at all. The Intelsat satellites serve a function—and thus produce "values"—only because of what the Court of Appeal termed their "invisible, but . . . continuous and very real, connection" with the earth stations to and from which they relay communication signals. It is therefore appropriate to assign income which Comsat derives from the use of the satellites to those jurisdictions where Comsat maintains

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[10]Comsat also argues that the Board's formula produces a result which is out of all proportion to the business transacted by Comsat within the state. Juris. Stmt., at 15-16. This is not an independent argument since the "disproportion" between the Board's figures and the business attributed to California by Comsat results from the Board's treatment of the space segment assets. As for the amount of income apportioned to California by the Board, as compared to the relative extent of lease activity at the California earth station, see *supra*, at 10.

earth stations and makes the satellite communications system available to terrestrial carriers.[11]

Comstat has termed this approach "California's 'invisible connection' theory." Juris. Stmt., at 18. It claims that the Court of Appeal's decision has "vast implications in the field of telecommunications and beyond," stating:

> "... California could, under the court's view, properly tax income generated by telecommunications equipment located outside California, as well as other equipment such as computers, which communicate with facilities in California. The rationale that the court below applied to satellites in outer space would be equally applicable to a microwave tower in

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[11]The tremendous importance which the earth stations have in the production of Comsat's income was recognized in a statement attributed to a former Comsat executive. He was quoted as saying:

> "What is Comsat selling? The law says it's selling 'channels of communications.' Without the earth station, there is no channel. If another guy has the earth station, you're selling him only the opportunity to look at a satellite, not a channel.
>
> "More important, do you see yourself as expanding into new areas, acting competitively? If you don't have control of distribution on the ground, how can you possibly sell your services?" (Quoted in Kinsley, *Outer Space and Inner Sanctums*, John Wiley & Sons (1976) at 36-37.)

The California earth station, in particular, was constructed because of the urgent need for an earth station in the Southwestern part of the United States so that efficient service could be provided through the satellite system. Stip., ¶27. The reasons for the selection of the specific site at Jamesburg, as stated in the FCC application for authority to construct the California earth station, were as follows:

> "It has been selected for its relative freedom from terrestrial system interference problems. The area is free from industrialization and has been developed with respect to power and water resources. Its close proximity to a good road, its location in a natural 'bowl,' and its temperate climate make it suitable for an earth station." Stip., ¶28.

> Oregon communicating with California." Juris. Stmt., at 17-18.

This, in a word, is nonsense.

Although Comsat is unwilling to concede the point, Intelsat satellites are unique in that, unlike telephone equipment in Reno, Nevada (or microwave towers in Oregon), they are located beyond the confines of any taxing jurisdiction. At the same time, though the satellites are located in outer space, they serve a function only on Earth. That function is performed at the earth stations which are "invisibly connected" to the satellites by virtue of the constant communication signals which the earth stations transmit to, and receive from, the satellites. The Court of Appeal properly concluded that to ascribe the satellite functions to the earth stations "is a recognition of the realities of telecommunications and space technology. . . ." Juris. Stmt. App. A-28 to A-29. Comsat is plainly wrong in suggesting that, in the court's view, California could give similar treatment to terrestrial equipment located in another taxing jurisdiction.

It is also untrue that "California has already carried its 'invisible connection' theory one step further by allocating to itself a share of the Intelsat revenues produced in part by ground tracking and control facilities located in other states and foreign countries on the notion that these facilities are 'invisibly connected' to the California earth station through the satellites." Juris. Stmt., at 18.[12] The

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[12] In more general terms, Comsat claims that there is not even a "minimal connection" or "nexus" between the State of California and the activities of Intelsat, whose revenues "Comsat shares independent of any privilege or authority granted by California." Juris. Stmt., at 14., see also Juris. Stmt., at 18. The California earth station, however, is part of the Intelsat network. Furthermore, as Comsat concedes, the income which it derives from its membership in Intelsat is "unitary income." See, e.g., Juris. Stmt., at 17. Given the existence of a unitary business,

Court of Appeal said nothing about the ground tracking and control facilities being "invisibly connected" to the California earth station. Furthermore, the out-of-state locations of these facilities have been taken into account in the Board's property factor, the value of the facilities having been included in the denominator but not the numerator of the fraction. See Stip., ¶ ¶ 43 and 56. This means, of course, that the property factor has attributed a portion of Comsat's share of the Intelsat revenues to the jurisdictions where the ground tracking and control facilities are located. In the case of the sales factor, on the other hand, the assignment is made on the basis of where and what the customer purchases. Thus, in this case, the Board has assigned Comsat's share of space segment revenues to those jurisdictions where Comsat leases half circuits between an earth station and one of the Intelsat satellites.

Comsat has also lost sight of the fact that the formula apportionment method "does not purport to identify the precise geographic source of a corporation's profits; rather it is employed as a rough approximation of a corporation's income that it reasonably related to activities conducted within the taxing State." *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273 (1978). Accordingly, it is incumbent upon a complaining taxpayer to establish that a particular formula *as a whole* has attributed an amount of income to the taxing state which is " 'out of all appropriate proportion to the business transacted . . . in the state' . . . or has 'led to a grossly distorted result'. . . ." *Id.*, at 274; citations omitted. In this phase of the case, therefore, Comsat would have to establish (which it has made no attempt to do) that the Board's

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"a State can gain a justification for its tax consideration of value that has no other connection with that State." *F.W. Woolworth Co. v. Taxation & Revenue Dept.*, 458 U.S. 354, 364 (1982).

formula has "grossly distorted" the amount of income attributable to California because the out-of-state locations of the ground tracking and control facilities have not been given sufficient weight in the property factor alone.[13]

B. The Board's formula comports with the Due Process Clause, even if it is assumed that some values are produced in outer space

Assuming, *arguendo*, that the Board's formula inevitably results in the taxation of "extraterritorial" values produced in outer space, the use of that formula would still not violate the Due Process Clause. Admittedly, there are innumerable opinions of this Court which declare that a state may not extend its taxing powers beyond its own borders. However, the maxim must be considered in context. As this Court admonished in *Wisconsin v. J.C. Penney. Co.*, 311 U.S. 435, 444-445 (1940):

> " . . . 'Taxable event,' 'jurisdiction to tax,' 'business situs,' 'extraterritoriality,' are all compendious ways of implying the impotence of state power because state power has nothing on which to operate. These tags are not instruments of adjudication but statements of a result in applying the sole constitutional test for a case like the present one. That test is whether property was taken without due process of law, or, if paraphrase we must, whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state.

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[13] Since Comsat serves as manager of all Intelsat space segment facilities, Stip., ¶ 13, it is likely that the out-of-state locations of these facilities also have been taken into account in Comsat's payroll factor. Little detail on this factor is available in the record since it has never been the subject of dispute.

> " . . . We must be on guard against imprisoning the taxing power of the states within formulas that are not compelled by the Constitution but merely represent judicial generalizations exceeding the concrete circumstances which they profess to summarize."

In a subsequent opinion, this Court stated:

> " . . . visible territorial boundaries do not always establish the limits of a state's taxing power or jurisdiction. . . . If there is some jurisdictional fact or event to serve as a conductor, the reach of the state's taxing power may be carried to objects of taxation beyond its borders. When it has the taxpayer within its power or jurisdiction, it may sometimes, through him, reach his extraterritorial income or transactions." *Miller Bros. v. Maryland*, 347 U.S. 340, 342-343 (1954).

Thus, the principle that a state is powerless to tax "extraterritorial" values is not without exception, and as far as the Board is aware, has never been applied to create a total immunity from any taxation by any jurisdiction. Rather, restraints generally have been imposed on the states in order to avoid multiple taxation, while at the same time holding the taxpayer accountable to some taxing jurisdiction. Perhaps the best illustration of this is found in the rule dealing with *ad valorem* taxation of vessels plying the high seas. It was held at an early date that such a vessel could be taxed by the state of the owner's domicile even though the vessel was never physically located there. See *Southern Pac. Co. v. Kentucky*, 222 U.S. 63 (1911). The rule was applied to insure "that a vessel, while protected from multiple taxation, [should] not escape taxation altogether." Note, 11 Stan. L. Rev. 581, 522, n. 19 (1959); see also *Standard Oil Co. v. Peck*,

342 U.S. 382, 388 (1953) (Justice Minton, dissenting); *Ott v. Mississippi Barge Line*, 336 U.S. 169 (1949).

The above cases were concerned with the "situs" of property for purposes of *ad valorem* taxation. For present purposes, however, they illustrate the fact that this Court has been unwilling to immunize a business enterprise from taxation by a state to which it owes some allegience unless, and to the extent that, it may be taxable elsewhere.

The controlling constitutional principle is that "[a] state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society." *Wisconsin v. J.C. Penney Co., supra*, at 444. Clearly, the only civilized societies which enable Comsat to function and profit as a business concern are those Earthly jurisdictions which have some hand in its operations. Comsat has been able to realize income from the satellites only because of the essential services provided by California and its sister states.

In sum, the apportionment formula employed by the Board is designed to reflect the amount of protection, benefits and opportunities afforded by California in relation to the total amount of protection, benefits and opportunities afforded to Comsat everywhere. It thus comports with the Due Process Clause. To paraphrase this Court in the *Wisconsin* case: "Here the incidence of the tax as well as its measure is tied to the earnings which the State of California has made possible, insofar as government is the prerequisite for the fruits of civilization for which, as Mr. Justice Holmes was fond of saying, we pay taxes." See 311 U.S., at 446.

II

COMSAT'S EQUAL PROTECTION AND COMMERCE CLAUSE ARGUMENTS ARE ALSO DEVOID OF MERIT

Comsat points out that the Board has "admitted" that the particular formula it used here has not been applied to any other taxpayer, Juris. Stmt., at 8, and then goes on to claim that "[t]he Board's failure to apply its rationale to comparable telecommunications companies is at odds with the values inherent in the Equal Protection Clause." Juris. Stmt., at 21. The admission of the Board is hardly surprising in view of the fact that Comsat is the only company in the United States which is authorized to engage in the international satellite communications system. 47 U.S.C.A. § 731 et seq. No other American company has an interest in the Intelsat satellites. No other American company derives income from the lease of half circuits in the Intelsat network. At least during the years in question, Comsat was also a pioneer in a wholly new industry.[14]

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[14] Earlier, Comsat says that one of the questions presented in the case is whether a state may constitutionally substitute a special formula for "the benchmark three-factor statutory formula." Juris. Stmt., at 11. Aside from the fact that the Court of Appeal found that the Board's formula was consistent with the statutory formula, see *supra*, at 5, 9-10, the alleged issue is a curious one. This Court has repeatedly held that in calculating in-state values, "the Constitution imposes no single formula on the States." *Container Corp. of America v. Franchise Tax Board*, *supra*, 103 S. Ct., at 2939.

The difficulty of a literal application of the standard formula to businesses similar to that conducted by Comsat is recognized in the regulations issued by the Multistate Tax Commission. Regulation IV.18(a), as adopted by California, provides in relevant part:

> "In the case of certain industries such as air transportation, rail transportation, ship transportation, trucking, television, radio, motion pictures, various types of professional athletics, and so forth, the foregoing regulations in respect to the apportionment formula

Furthermore, Comsat has neglected to mention that lessees of its California half circuits have been taxed on a comparable basis. During the years in question, four common carriers doing business in California were identified as lessees of Comsat, three of which had been audited. See Stip., ¶38; Pl. Exh. 4. In two instances, the property factor for the lessee was analogous to the property factor for Comsat; it reflected the capitalized rentals for California half circuits in the numerator and all of the lessee's property in the denominator. Pl. Exh. 4. In the third instance, only property physically located in California was included in the numerator and only property located in other jurisdictions was included in the denominator. *Id.* The end result of either factor was, of course, the same. In order to avoid the attribution of income to outer space, it is necessary either to "throwout" a taxpayer's space-related activities or "throw back" those activities to the jurisdictions where the taxpayer is engaged in business.

Comsat claims that other property located outside California is not considered to be "used" in California, and "there is no rational basis or legitimate state purpose for making a distinction based upon the type of property outside California which generates the income." Juris. Stmt., at 20. It is not really the "type" of property but where it is located which furnishes the basis for a valid distinction in the present case. If the satellites were located in New Mexico instead of outer space, all sorts of constitutional restraints would come into play because

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do not set forth appropriate procedures for determining the apportionment factors. Nothing in section 25137 or in this Regulation shall preclude the Franchise Tax Board from establishing appropriate procedures under sections 25129 to 25136 inclusive for determining the apportionment factors for such industries, but such procedures shall be applied uniformly." 18 Cal. Admin. Code §25137.

New Mexico would be furnishing protections and benefits to Comsat for which it too would be entitled to ask some return. The satellites are not located in New Mexico, they are located in outer space. The Equal Protection Clause is not violated where a distinction is based on such constitutional differences. See, e.g., *Matson Nav. Co. v. State Board*, 297 U.S. 441, 446 (1936); *Union Bank & Trust Co. v. Phelps*, 288 U.S. 181, 187 (1932).

Finally, the Board's formula is not open to the Commerce Clause objections raised by Comsat. As Comsat's quotation from *Armco Inc. v. Hardisty*, ____ U.S. ____, 104 S. Ct. 2620 (1984) pointedly indicates, "A tax that unfairly apportions income *from other States* is a form of discrimination against interstate commerce." 104 S. Ct., at 2624; emphasis added. There has been no showing here that the formula employed by the Board has resulted in an unfair apportionment of income earned by Comsat in other states. Each of the other tests articulated in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), which substantially track the due process requirements, have also been satisfied.

III

AN APPEAL IN A CASE RAISING SUBSTANTIALLY THE SAME ISSUE WAS RECENTLY DISMISSED BY THIS COURT FOR WANT OF A SUBSTANTIAL FEDERAL QUESTION

The fundamental issue in this case is essentially the same as that recently presented to this Court in the appeal of *Sjong v. State Dept. of Revenue*, Alaska, 622 P. 2d 967 (1981). This Court dismissed that appeal for want of a substantial federal question. 454 U.S. 1131 (1982).

The taxpayer in *Sjong* was a commercial crab fisherman who fished exclusively in the international waters surrounding Alaska. His vessel was licensed, registered and harbored in the State of Washington; he outfitted his vessel and hired his crew in Seattle; and all of his sales were negotiated in Washington. During the commercial fishing season, however, he came to an Alaskan port once every 10 to 15 days to deliver his catch to a processing plant. While in port, he obtained supplies which enabled him to continue his fishing activities. He also entered Alaskan ports to obtain emergency medical treatment for ailing crew members or to have emergency repairs performed on his vessel. Using a port-day formula, the Alaskan taxing authorities apportioned approximately 85 to 92 percent of Sjong's income from the crab sales to Alaska, though about 95 percent of his business activity (including the activity in international waters) was outside the state.

Sjong contended that the apportionment formula was manifestly unfair and argued, among other things, that the services and benefits provided to him by Alaska were available to any person traveling interstate and should not be the basis for the imposition of a tax. In answering this argument, the Supreme Court of Alaska stated:

> "...What must be recognized, however, is that unlike the services rendered to an ordinary traveler, the services, benefits and protections offered to Sjong are directly related to generating his income. Without the opportunity to purchase fresh bait and supplies, he would be severly hampered in his ability to continue his fishing ventures. Further, the availability of emergency medical services, repair facilities, and crew replacement in Alaska clearly benefits his business operations, as does the opportunity to sell

his crab without the expenditure and delay of a lengthy trip.

"It is precisely this notion, that the benefits afforded to the taxpayer are directly related to 'business income generation,' which is central to a resolution of this case." 622 P. 2d, at 980.

Sjong filed an appeal with this Court. *(Sjong v. State of Alaska.* No. 81-504.) The issues presented were:

"1. Does the State lack the sufficiently substantial nexus to appellant's activities required by the commerce and fourteenth amendment due process clauses to tax his net income derived from [sales of crab caught exclusively in international waters]?

"2. Is an allocation to the taxing state of 85-92% of net income derived from such sales a fair apportionment under the commerce and fourteenth amendment due process and equal protection clauses where appellant conducts only a small percentage of his business activities within the taxing state?" Jurisdictional Statement, *Sjong v. State of Alaska,* No. 81-504, at i.

This Court determined that the questions presented in *Sjong* were so unsubstantial as not to require further argument. The circumstances in the case at hand are analogous. See also *Matson Nav. Co. v. State Board of Equalization,* 3 Cal. 2d 1, 43 P. 2d 805 (1935), aff'd 297 U.S. 441 (1936) (income of a shipping company engaged in interstate and foreign commerce on the high seas apportioned on the basis of "business originating" in California as compared to "business originating" elsewhere).

CONCLUSION

This case presents an intriguing factual situation. However, as Comsat correctly points out, the governing constitutional principles were established long before the advent of space technology. Under these governing principles, the income of a multistate corporation may be taxed on the basis of a formula which fairly apportions that income among those jurisdictions where the corporation conducts its business activities. Accordingly, it is respectfully submitted that this Court should dismiss this appeal or, in the alternative, affirm the decision of the California Court of Appeal.

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Respectfully submitted,

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